Financial Literacy throughout the Life Cycle

A Mini-Conference of the 2005 White House Conference on Aging

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Breakout Group Two – Building a Financially Secure Society

What Can Be Done to Help Americans Optimally Manage Financial Assets throughout Life?

The White House Conference on Aging should support policies that:

Include materials in federal government mailings such as Social Security statements and tax forms that provide information about retirement asset management issues that can protect older people against the financial risks associated with living longer than normal life expectancy. This could include information on life expectancy, health enhancement, budgeting, income planning, life annuities, long-term care insurance, and other issues. Social Security mailings are a highly efficient mechanism for reaching the retired population. Considering the need to integrate investing and spending plans with Social Security benefits information from the Social Security administration on retirement asset management could be highly effective.

Encourage community-based and nonprofit organizations such as colleges and universities, senior centers, religious institutions, libraries, and others to provide retirement asset management advice and education to retirees and near retirees. Many people have trusted relationships with a wide range of organizations and institutions. As they are receptive to information and advice from these sources, these organizations and institutions could be very helpful in educating about retirement asset management.

Encourage defined contribution plans to offer distribution options, such as life annuities, that provide a consistent and permanent stream of payments as a distribution option. The ultimate purpose of a retirement plan is to help employees gain a financially secure retirement. These distribution options can add to the financial security of many people, yet it is generally not offered. Making this product available as a distribution option in a defined contribution plan can serve to increase life risk protection and discourage early spend down.

Create incentives that encourage people to choose investments in retirement and distribution options that provide a consistent and permanent stream of payments, such as life annuities. Tax preferences have been proven effective in encouraging behavior, including encouraging the choice of distribution options. More use of these products could lead to less depletion of assets later in life, and therefore a lower burden placed on social support systems.

Revise regulations and laws that make it difficult for employers to offer distribution options that provide a consistent and permanent stream of payments, like life annuities, and have the government consider creating a re-insurance mechanism to make these options attractive and affordable to individuals. Some ERISA-based requirements make it harder for employers to offer and administer these distribution options. These should be re-examined and revised.

Create incentives that encourage people to buy long-term care insurance. People without long-term care insurance are more likely to have their financial resources depleted, cause spousal impoverishment, and fall back on Medicaid. Each of these impacts has social costs. Tax incentives can be effective in motivating higher purchase levels for long-term care insurance.

Encourage employers to default employees into a multi-sector diversified investment fund rather than a money market fund. These funds would have an asset allocation appropriate to the employee's age. Each would include a mix of investments, including life annuities, appropriate to the retiree's age and would automatically re-balance and shift asset mix as the retiree ages. These types of funds have been effective among a segment of the population who are not confident about selecting their own investments. Considering the lack of confidence that many who reach retirement have about investing without the aid of advice provided at the workplace, these funds could be an ideal solution for a key segment of the population.

Encourage the use of reverse annuity mortgages. Retired people have a substantial level of home equity. Reverse annuity mortgages can be an effective product to help people gain income from the equity in their home, without having to move out of their home or be disrupted in any way. Currently, awareness of reverse annuity mortgages is not high, preventing some people who could receive strong benefits from the product from obtaining it. Make the public more aware of the current Centers for Medicare & Medicaid Services (CMS) and Housing and Urban Development (HUD) programs to encourage reverse annuity mortgages.

Encourage employers to provide retirement asset management advice, programs and tools to employees. The worksite is a highly effective place to educate people about finances. There is evidence that employees tend to have confidence in advisors and firms selected by their employers. Information and advice provided at the workplace on retirement plans has had an impact on saving and asset allocation behavior. The workplace is one of the most effective and efficient places to provide advice on retirement asset management, especially among firms that have retirement or pension plans.

Permit greater flexibility for the requirement to take minimum distributions from IRAs and defined contribution plans. Currently, people must start taking income, and pay taxes, on IRAs and defined contribution plans at age 70½. At that age a number of people can have up to 30 years, or more, of life. It would be most helpful to their long-term financial security if these people could continue to hold money in these plans on a tax-deferred basis for a longer period of time. With increasing life expectancy and higher costs in later life, the requirement for taking minimum distributions at age 70½ should be re-examined.

Background Information

1. Life expectancy at age 65 has been going up rapidly and further increases are expected.
2. Individuals are increasingly responsible for managing their money in retirement due to a movement away from annuitized payments from defined benefit plans and toward defined contribution plans and cash balance plans.
3. The replacement ratios provided by Social Security will go down due to major increases in Medicare Part B premium (which comes directly out of Social Security), an increasing proportion of workers being exposed to the taxation of Social Security benefits, and higher tax levels due to the fact that the income threshold for the taxation of benefits is not indexed for inflation and the age of entitlement for full benefits is going up.
4. The increasing cost of health care will put greater financial strains on older people.
5. No cost family provision of long-term care services to older people will probably be less prevalent, due to smaller families, increased labor force participation of women, and increasing numbers of people with no children, requiring more costs for long-term care to be borne by the elderly.
6. Financial literacy studies indicate many people do not have strong money management skills even in later life.
7. Many people within 10 years of retirement appear to have underfunded their retirement accumulation and many people who have just entered retirement appear to not have enough

financial resources to avoid financial strain during their retirement. This makes effective asset management crucial to the maintenance of financial security. A significant segment of the old have depleted all, or almost all, of their financial resources.